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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

PERIODS ENDED JUNE 30, 1990

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MONTANA LOTTERY

FINANCIAL STATEMENTS
(Unaudited)

PERIODS ENDED JUNE 30, 1990

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APPOINTIVE OFFICIALS

Zoann Attwood, Lottery Director

L. John Onstad, Lottery Assistant Director for Security

LOTTERY COMMISSION

		TERM EXPIRES
Pat DeVries, Chairwoman	Polson	January 1, 1991
Becky Erickson	Glasgow	January 1, 1993
Gary Rebal	Great Falls	January 1, 1994
Ward Shanahan	Helena	January 1, 1994
Bill Ware	Helena	January 1, 1993

LOTTERY LIAISON COMMITTEE

Senator Hubert Abrams	Wibaux
Senator Ethel Harding	Polson
Representative Linda Nelson	Medicine Lake
Representative Norman Wallin	Bozeman

REPORT DISTRIBUTION

According to Section 23-5-1007(7), MCA, copies of this report must be distributed to the following individuals.

Stan Stephens, Governor

Dave Ashley, Director, Department of Administration

Scott Seacat, Legislative Auditor

Jack Galt, President of the Senate

John Vincent, Speaker of the House

The law also states "the President of the Senate and the Speaker of the House will determine the report distribution to each member of the appropriate committee of each house of the legislature". The President of the Senate and the Speaker of the House requested this report be distributed to the Revenue Oversight Committee. In addition, the Speaker of the House requested this report be distributed to the House Business and Economic Development Committee.

Members of the Revenue Oversight Committee include:

Senators	Representatives
Bill Norman, Chairman	Susan Good, Vice Chairman
Bruce Crippen	Dan Harrington
Dorothy Eck	Robert Hoffman
Thomas Hager	Jim Patterson
Joe Mazurek	Ted Schye
Robert Brown	Robert Ream

The House Business and Economic Development Committee members include:

Representatives	
Bob Pavlovich, Chairman	Gene DeMars, Vice Chairman
Fred Thomas	Bob Bachini
William Glaser	Thomas Nelson
Stella Jean Hansen	Lloyd "Mac" McCormick
Bruce Simon	Norm Wallin
Clyde Smith	Rob Blotkamp
John Johnson	Vernon Keller
Tom Kilpatrick	Don Stappler

October 31, 1990

Montana Lottery Commission:

The fourth quarter of fiscal year 1990 continued along this fiscal year's trend of increased revenue and profit. Each quarter in fiscal year 1990 has had revenue higher than the previous quarter. In addition, the fourth quarter's $1.5 million transfer to the Office of Public Instruction (OPI) was the third highest transfer ever.

This was a fine ending to a very successful fiscal year. The addition of our Lotto*America product added revenue and profit, and at the same time, our instant ticket revenue held steady.

Also, during this quarter I joined the Lottery as Director, and find myself with the challenge to keep the Lottery moving along this positive and exciting direction.

With nearly $4.2 million transferred to OPI in fiscal year 1990, there is a good base to build upon for the coming fiscal years.

Zoann Attwood

Zoann Attwood
Director

MONTANA LOTTERY
BALANCE SHEET
JUNE 30, 1990

ASSETS	(Unaudited)
Cash	$ 516,735
Investment in Short-Term Investment Pool	824,500
Receivables (Net)	771,995
Inventories	108,456
Equipment	768,090
Other Fixed Assets	4,093
Accumulated Depreciation	(341,803)
Intangible Assets	388,284
Other Assets	7,868
TOTAL ASSETS	$ 3,048,218

LIABILITIES AND FUND EQUITY	
Liabilities:	
Accounts Payable and Accruals	$ 335,438
Lottery Prizes Payable	695,145
Due to Other Funds (Note 2)	1,590,037
Deferred Revenue	20,029
Installment Purchase/Lease Payable	165,284
Compensated Absences Payable (Note 1)	94,392
Allowance for Ticket Returns	147,893
	$ 3,048,218
FUND EQUITY:	
Retained Earnings Unreserved	-0-
Total Fund Equity	-0-
TOTAL LIABILITIES AND FUND EQUITY	$ 3,048,218

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN RETAINED EARNINGS
PERIODS ENDED JUNE 30, 1990

	Quarter Ended June 30, 1990 (Unaudited)	Twelve Months Ended June 30, 1990 (Unaudited)
OPERATING REVENUES:		
Charges for Service		
Net lottery ticket revenue	$ 7,016,283	$ 21,502,463
Revenue from other sources	6,039	6,039
Sold Instabucks (net)	(28)	1,335
License and permits	950	4,150
Interest Earnings on STIP	9,762	25,773
Total Operating Revenues	$ 7,033,006	$ 21,539,760
Prizes and Commissions		
Prize expense	(3,235,504)	(10,189,328)
Retailer commission	(412,092)	(1,352,477)
Net Operating Revenue	$ 3,385,410	$ 9,997,955
OPERATING EXPENSES:		
Amortization	$ 51,187	$ 204,747
Personal Services	223,033	919,490
Contractual Services	1,076,879	2,677,769
Cost of tickets sold	162,790	552,884
Audit Fees	17,101	45,044
Supplies and Materials	55,224	103,051
Depreciation	32,239	118,258
Utilities and Rent	23,700	95,280
Communications	26,838	67,710
Advertising	124,610	779,968
Travel	11,336	41,706
Repairs and Maintenance	27,062	83,709
Management Service Fee	29,045	78,172
Other	4,749	60,740
Total Operating Expense	$ 1,865,793	$ 5,828,528
Operating Income	$ 1,519,617	$ 4,169,427
NONOPERATING REVENUES (EXPENSES)		
Interest Expense	(96)	(540)
Total Nonoperating Revenues (Expense)	(96)	(540)
Income before Operating Transfers	1,519,521	4,168,887
Operating Transfers In (Out)	(1,519,521)	(4,168,858)
NET INCOME (LOSS)	$ -0-	$ 29
Retained Earnings, Beginning of Period (Note 5)		(29)
RETAINED EARNINGS, END OF PERIOD		-0-

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
Notes to the Financial Statements (Unaudited)
JUNE 30, 1990

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-5-1001, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and prepare financial reports.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the governmental Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Investment in Short-Term Investment Pool. The Short-Term Investment Pool (STIP) is a pool of investments, maintained by the Montana Board of Investments, with maturities of one year or less. The Lottery's purchase of units in STIP totalled $824,500 as of June 30, 1990. These funds are highly liquid and may be purchased or sold daily. Interest earnings accrue daily and income is distributed monthly. Interest earnings as of June 30, 1990 totalled $25,773.

Receivables. Receivables totalling $771,995 represent amounts owing the Lottery for purchased tickets. An allowance for doubtful accounts is usually based on historical perspective. Because of immaterial uncollectible account balances, an allowance for doubtful accounts has not been established.

Receivables include a $2,526 adjustment in retailer commissions related to estimated ticket returns.

Inventories. Inventories consist of merchandise, Instabuck and supplies inventories. Merchandise inventory includes lottery tickets valued at $92,100 stored in the warehouse and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold when sold. After game end and awaiting disposal, unsold tickets are charged to cost of tickets sold.

Merchandise inventory includes a $1,385 adjustment related to estimated ticket returns.

Supplies inventories include paper supplies, ticket dispensers, premiums and point-of-sale materials having a value of $5,000 or more. At quarter end, supplies inventories totaled $16,356. These inventories are also recorded at cost using the specific identification method.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's payable for compensated balances is detailed below.

Balance June 30, 1989	Net Leave Earned/Used	Balance June 30, 1990
$74,789	$19,603	$94,392

Allowance for Ticket Returns. This allowance represents a liability as of June 30, 1990 for estimated ticket returns. The allowance for ticket returns was increased by $53,259 from the quarter ending March 31, 1990. This is an estimate based, partially, on actual returns received after the end of the quarter. Conversely, ticket revenue has been decreased by approximately $53,259 for the quarter ended June 30, 1990. Prize expense has been decreased by approximately $25,869. Commissions and cost of goods sold have also been decreased for expenses associated with this change in allowance.

Revenue Recognition. Lottery instant ticket sales are recorded as revenue based on ticket deliveries to the retailers. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Lottery on-line ticket sales are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as deferred revenue until such time as the tickets become valid for the most current drawing.

Revenue From Other Sources. The Lottery has recognized $5,700 in anticipated revenue to be received based on an insurance claim filed with the Lottery's landlord's insurance agency. The claim arose out of damage sustained in the warehouse on October 25, 1989 when the sprinkler system malfunctioned damaging the warehouse and supplies inventory held in the warehouse. As of June 30, 1990, the Lottery had expensed approximately $5,700 to replace inventory and clean up the warehouse.

Other sources of revenue include recovery of a bad debt written off in a previous fiscal year.

Free Tickets. The Montana Lottery's instant games award free tickets as prizes. Net lottery ticket revenue does not include the value of free tickets given away and free plays won. The face value of these free tickets distributed approximated $412,564 for the quarter ended June 30, 1990.

Instabucks. Instabucks are a Lottery coupon good, upon redemption, for a lottery ticket. Instabucks, used to stimulate lottery ticket sales, are usually given away for promotions, retailer clerk incentive programs, and advertising trade-outs. The lottery tickets distributed resulting from Instabuck redemptions are reflected as a reduction in revenue. The related prize expense and ticket cost are reclassified as an advertising expense. For the quarter ended June 30, 1990, Instabuck redemptions resulted in a revenue reduction of $137,297 and a prize expense reclassification of $71,798.

Instabucks Sold. The Montana Lottery entered into an agreement with the Big Sky Country GMC Truck Dealers Association during the first quarter of fiscal year 1990 for the sale of 5,000 Instabucks to be used by the members of the association for promotional purposes during the "Pickup Plenty" instant ticket game. The sale and redemption of these Instabucks resulted in additional revenue to the Montana Lottery of $1,335.

Prizes. Expenses for instant prizes are recorded based on the predetermined prize structure for each game. No prize expense is recorded for free tickets distributed.

Expenses for on-line prizes are recorded based on the predetermined prize structure for the on-line game.

Commissions. Retailers receive a five percent commission on tickets or chances sold. Commission expense is recorded based on the face value of tickets delivered to the retailers and on the amount of revenue recorded for each on-line drawing.

Retailers can receive bonus commissions on tickets sold based on incremental sales of instant tickets. During the quarter ended June 30, 1990, retailers earned bonus commissions totaling $38,908.

Amortization. The Instant Lottery System (ILS) software, classified as an intangible asset, is being amortized over a period of five years using the straight line method. The Media Drop-In Productions, Inc. contract for the use of ten lottery advertisements, is also classified as an intangible asset. This contract is being amortized over a period of 3 years using the straight line method.

2. DUE TO OTHER FUNDS

The account "Due to Other Funds" totalling $1,590,037 reflects the $1,519,521 payable to the State Superintendent of Public Instruction and $70,516 due to other state agencies for goods and services provided through June 30, 1990.

3. PAID PRIZES

Section 23-5-1027 MCA states "A minimum of 45% of the money paid for tickets or chances must be paid as prize money".

For the quarter ended June 30, 1990, the prize expense of $3,235,504 reflects 46.11% of net ticket revenues totalling $7,016,283. From April 1, 1990 through June 30, 1990 prizes paid are detailed as follows:

High-tier	$ 638,360
Low-tier	1,051,212
Big Win	257,000
On-line	2,075,535
	$4,022,107

High-tier prizes reflect prizes greater than $25 paid through Lottery headquarters. Low-tier prizes of $25 or less are paid by the retailer or Lottery headquarters.

4. TRANSFER TO STATE SUPERINTENDENT OF PUBLIC INSTRUCTION

Section 23-5-1027, MCA states "that part of all gross revenue not used for payment of prizes, commissions, and operating expenses is net revenue and must be paid quarterly from the enterprise fund to the State Superintendent of Public Instruction for distribution as equalization aid to the public schools of Montana..." For the quarter ended June 30, 1990, the net revenue amounted to $1,519,521.

5. DEFICIT RETAINED EARNINGS

According to the law, the Lottery's net revenue must be transferred quarterly to the State Superintendent of Public Instruction. This transfer should result in a zero retained earnings balance. Because of recording a fiscal year 1988-1989 expenditure after calculation of the transfer for the quarter ending June 30, 1989, the beginning retained earnings balance is (29) rather than zero.

6. PRIZE RESERVE FUND

As a member of the Multi-State Lottery Association (MUSL) and the Lotto*America game, the Lottery is required to contribute to a prize reserve fund maintained by MUSL. This fund is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund, as well as the interest earned on the Lottery's share of the fund, would be returned to the Lottery upon leaving MUSL (assuming that no unanticipated prize claims have been paid).

The Lottery contributes to the reserve fund through the 45% set-aside for prizes. In addition the Lottery is required to contribute for its portion of the reserve fund accumulated since the start of the Lotto*America game. The Lottery has chosen to do so by paying an additional 2% of drawing revenue rather than making a lump sum payment. Payments made to this fund are considered a portion of the prize expense associated with the on-line game. Contributions to this fund total $352,410, interest earnings equal $13,337 for a total of $365,747 as of June 30, 1990.

7. GAMES

Currently, the Montana Lottery games are instant ticket games and an on-line game referred to as Lotto*America. Instant ticket games provide players the opportunity to win instantly by scratching a latex covering to reveal a prize. Players also have another chance to win by submitting five non-winning tickets or their equivalent for the Big Win drawing. The Lotto*America game allows players the chance to win a minimum of $2 million. Players select 6 numbers from a field of 54 and must match at least 4 out of 6 to win. Drawings are held twice weekly on Wednesday and Saturday nights. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

8. GAMING SUPPLIER CONTRACTS

Tickets. On March 9, 1990, the Montana Lottery entered into a one year contract with Dittler Brothers, Inc. to purchase lottery tickets.

The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure. The contract requires payment within 30 days of ticket receipt.

Dittler Brothers, Inc., as the vendor, delivered a $500,000 performance bond covering the contract term. The Company also provided an errors and omissions policy covering an ultimate net loss of $4,500,000.

This contract may be terminated when termination is in the best interest of the Lottery with proper notification to Dittler Brothers, Inc.

Computer Hardware and Software. The Lottery contracted with Scientific Games, Inc. on February 25, 1987, to purchase a used Stratus computer. The computer hardware and software cost $381,243. This contract also covered the acquisition of an Uninterruptable Power Supply (UPS) system for $40,551. The UPS system protects the computer against electrical power surges and failures.

The Lottery signed a separate agreement with Stratus Computer, Inc. on June 2, 1987, for maintenance of the Stratus computer hardware and software. Monthly maintenance totals $4,433.

On July 28, 1987, the Lottery signed a second agreement with Stratus Computer, Inc. regarding the Stratus software license. Under this contract, Stratus Computer, Inc. grants the Lottery a "nonexclusive, nontransferable license" to use the software of the Stratus computer. The proprietary rights and title of the software remain with Stratus Computer, Inc.

Lottery Software. On February 25, 1987, the Lottery agreed to purchase the Instant Lottery System (ILS) software package for $840,400. This agreement provides the Lottery a "perpetual, nonexclusive, nontransferable license to use the software solely for the Lottery's own use". The contract allows the Lottery to make 36 monthly payments of $23,344.44 with no interest. The first payment was due June, 1987.

Under the Extension and Second Amendment of Instant Ticket Contract dated January 5, 1989, these monthly payments were reduced to $11,672.22 commencing with the November 1988 payment. Upon expiration or termination of the Instant Ticket Contract with Scientific Games, Inc. on March 8, 1990, the payments were reinstated to $23,344.44 until the balance is paid in full.

On-line Services. On August 30, 1989, the Lottery contracted with Control Data Corporation to provide on-line terminals, central computers, telecommunications network, and training for a five year period. The contract, with an effective date of November 9, 1989, provides that payment will be a percentage of sales, which for the first year of the contract will be 25% of the first $250,000 of weekly sales, and 19% for sales between $250,001 to $500,000. The percentage decreases with higher weekly sales.

Control Data Corporation, as the vendor, delivered a $1,250,000 performance bond covering the contract term.

9. PRIZE ANNUITIES

During fiscal year 1989, the Montana Lottery awarded four Big Spin Jackpot prizes totalling $5,000,000. The Lottery made the initial payments to the winners in the amount of $253,088 and on September 26, 1988, the Montana Lottery awarded annuities in the amount of $2,350,180 to Western National Life. Through these annuities, Western National Life makes the remaining payments to the Big Spin Jackpot winners. As of June 30, 1990, the contingent liability for future prize payments funded through the purchase of annuities was $4,240,735.

10. LOTTO*AMERICA JACKPOT PRIZES

Jackpot prizes awarded in the Lotto*America game are funded through the purchase of U.S. Treasury Zero-Coupon Bonds purchased in the name of the Montana Lottery by MUSL. MUSL will cash the bonds each year as they mature and will wire the funds to the Lottery for payment to winners on the anniversary date of the win.

On January 13, 1990, the Montana Lottery awarded its first Lotto*America jackpot prize totalling $1,740,000. The first annual payment of $87,000 was made on February 1, 1990. On May 9, 1990, the Lottery awarded a second Lotto*America

jackpot prize of $3,000,000. The first annual payment of $150,000 was made on May 23, 1990. As of June 30, 1990, the contingent liability for future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds was $4,503,000.

OTHER

INFORMATION

MONTANA LOTTERY
SUMMARY OF FINANCIAL DISTRIBUTION
(UNAUDITED)
PERIODS ENDED JUNE 30, 1990

COMMISSIONS - Section 23-5-1016(10), MCA provides retailers a 5% commission on instant and on-line tickets or chances sold. The commission on tickets sold to the retailer gives the retailer $15 per book of 300 tickets or $15 per 300 on-line tickets sold. The 5% commission of $412,092 and $1,352,477 for the quarter and twelve months ended June 30, 1990, is based on gross lottery ticket sales of $7,619,252 and $23,793,973. In addition retailers earned bonus commissions on tickets or chances sold of $38,908 during the quarter for a total of $160,939 in bonus commissions paid during the twelve months ended June 30, 1990.

OPERATING EXPENSES - The Lottery, according to Section 23-5-1007(9), MCA, must prepare quarterly and annual reports on all aspects of the operation of the state lottery, including gross revenue and operating expenses. Gross revenue includes net lottery ticket revenue and license fees. While retailer commissions, by law, are not considered an operating expense, interest expense is considered an operating expense for this purpose. The operating expenses for the quarter and twelve months ended June 30, 1990, using the accrual basis of accounting, are as follows:

	Quarter ended June 30, 1990 (Unaudited)	Twelve Months ended June 30, 1990 (Unaudited)
Net lottery ticket revenue	$ 7,016,283	$21,502,463
Revenue from other sources	6,039	6,039
Sold Instabucks	(28)	1,335
License and permits	950	4,150
Interest Earned on Investments	9,762	25,773
Total Gross Revenue	$ 7,033,006	$21,539,760
Operating expenses	1,865,793	5,828,528
Interest expense	96	540
Total Operating Expense	$ 1,865,697	$ 5,827,988

STATE SUPERINTENDENT OF PUBLIC INSTRUCTION TRANSFER - The funds transferred to the State Superintendent of Public Instruction, by law, are not based on a percentage of revenue. The distribution is based on a definition of net revenue. Net revenue is that part of all gross revenue not used for the payment of prizes, commissions, and operating expenses. Net revenue for the quarter and twelve months ended June 30, 1990, is detailed below:

	Quarter ended June 30, 1990 (Unaudited)	Twelve Months ended June 30, 1990 (Unaudited)
Income before Operating Transfers	$1,519,521	$4,168,887
Retained Earnings, Beginning of Period	-0-	(29)
Net Revenue Transferred to State Superintendent of Public Instruction	$1,519,521	$4,168,858

PRIZES - Section 23-5-1027(1a), MCA, states "A minimum of 45% of the money paid for tickets or chances must be paid out as prize money..."

Prize expense is recorded based on the predetermined prize structure percentage for each game. For the quarter ended June 30, 1990, the prize expense of $3,235,504 is 46.11% of net Lottery ticket revenue of $7,016,283. For the twelve months ended June 30, 1990, the prize expense of $10,189,328 is 47.38% of the net Lottery revenue of $21,502,463.

When recording the prize expense, a corresponding liability for high-tier and, if applicable, Big Win prizes is also recorded. The relationship between prize expense, prizes paid and the change within prize liability is illustrated below:

April 1 through June 30, 1990		Percent of Net Lottery Ticket Revenue (Unaudited)
Prizes paid	3,972,425	56.62
Instabucks	(71,798)	(1.03)
Increase (decrease) in prize liability	(665,123)	(9.48)
Prize expense	$3,235,504	46.11

July 1 through June 30, 1990		Percent of Net Lottery Ticket Revenue (Unaudited)
Prizes paid	11,149,359	51.85
Instabucks	(150,033)	(.70)
Increase (decrease) in prize liability	(809,998)	(3.77)
Prize expense	$10,189,328	47.38